No. 3876

IN THE

United States Circuit Court of Appeals

FOR THE

NINTH CIRCUIT

17.

EWA PLANTATION COMPANY,
a Hawaiian Corporation,
Plaintiff-in-Error,

vs.

CHARLES T. WILDER,
as Tax Assessor for the First Taxation Division, Territory of Hawaii,
Defendant-in-Error.

BRIEF ON BEHALF OF PLAINTIFF-IN-ERROR

Upon Writ of Error to the Supreme Court of the Territory of Hawaii.

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SUBJECT INDEX

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STATEMENT OF THE CASE.

This case originated in the Supreme Court of Hawaii in the form of a "submission without action" upon agreed facts, the procedure being authorized by Sections 2381-2384, Revised Laws of Hawaii, 1915, as amended by Act 82 of the Session Laws of 1921.

On February 28, 1921, Ewa Plantation Company (plaintiff-in-error) filed with the tax assessor, as required by law, its annual income tax return showing its net income for the calendar year 1920. The tax

assessor questioned the correctness of the return in certain respects and the resulting differences of opinion were submitted to the Supreme Court for determination as above stated. The differences of opinion related to four items in the company's return, viz.: (1) Item 19 of Schedule "A" of the return designated "Strike Claim Settlement, $2,324,-931.75" which the assessor increased to $2,791,697.72, the agreed facts in connection therewith being set forth in the submission (Transcript of Record, pp. 2-6); (2) Item 2 in Schedule "B" of the return, designated "Interest on Mainland and Foreign Investments, $52,442.23" which the company claimed to be an allowable deduction from its gross income, but which the assessor refused to allow, the agreed facts in connection therewith being set forth in the submission (Record, pp. 6-8); (3) Item 15 (c) in said Schedule "B" designated "Loss on Sale Sugar Factors Stock $289,680.00"; and (4) Item 15 (d) in said schedule designated "Loss on Sale Miscellaneous Bonds, $197,824.11" (Record, pp. 8-13). The questions relating to these last two items were decided in accordance with the contentions made on behalf of the company (Record, pp. 48-54) so that they are not involved in this proceeding. Judgment was entered in the court below in favor of the assessor and against the company as to said Item 19 in Schedule "A", and as to Item 2 in Schedule "B", the total amount of the judgment being $20,768.28 (Record, pp. 64-66).

The opinion of the court below was included with its opinion in another case, Hawaiian Sugar Company vs. Charles T. Wilder, assessor, which was submitted at the same time as this case, but that case has not been brought to this court.

In that case there was involved a question as to the depreciation of a leasehold (Record, pp. 54-63) which was also the subject of an opinion by the court on a motion for a rehearing which is reported in 26 Haw. 356.

ERRORS RELIED ON.

The following errors have been assigned (Record, pp. 80, 81) and are now relied upon as reasons for the reversal of the judgment below, viz.:

1. That said Supreme Court erred in holding that the entire sum of $2,791,697.72 received by Ewa Plantation Company from the Hawaiian Sugar Planters' Association in 1920, by way of compensation for losses incurred by reason of the laborers' strike on the Island of Oahu, should be accounted for by said company as taxable income received during the year 1920.

2. That said Supreme Court erred in not holding that said sum of $2,791,697.72 should be apportioned and the respective parts thereof so apportioned taken into account for income taxation purposes when and as the crops to which such parts respectively ap-

pertained, viz., the crops of 1920, 1921 and 1922, shall have been sold and the net results ascertained with reference to each of said crops.

3. That said Supreme Court erred in holding that the doctrine of the maxim *mobilia sequuntur personam* has not been repudiated by judicial precedent in Hawaii with reference to taxation.

4. That said Supreme Court erred in not holding that even if said doctrine has not been so repudiated it should not be applied in this case under the circumstances set forth in paragraph 4 of the submission herein.

5. That said Supreme Court erred in holding that the case of Maguire vs. Trefry, 253 U. S. 12, is a controlling authority in the case at bar.

6. That said Supreme Court erred in holding that the sum of $52,442.23 received by Ewa Plantation Company during the year 1920 as interest upon foreign investments, i. e., interest on the bonds and notes of mainland railroad and industrial corporations and upon deposits in mainland banks, was not legally deductible in ascertaining the taxable income of said company in its tax return for 1921.

7. That said Supreme Court erred in holding that said sum of $52,442.23 constituted taxable income of said company.

8. That said Supreme Court erred in adjudging that the second sub-item under Item (19) of Schedule "A" of the income tax return of Ewa Plantation Company filed on February 28, 1921, relating

to the income of said company for the year 1920 returned at \$2,324,931.75 should be increased to \$2,791,697.72 and that the income taxes payable with reference to the said item be increased by the sum of \$18,670.60 over the amount shown by said company's said return.

9. That said Supreme Court erred in adjudging that the deduction claimed in Schedule "B" of the said income tax return of Ewa Plantation Company, viz., Item "(2) Interest on Mainland and Foreign Investments," should be disallowed and that the income taxes payable by said company with reference to the said item be increased by the sum of \$2,097.68 over the amount shown by said company's said return.

10. That said Supreme Court erred in rendering and entering judgment in favor of Charles T. Wilder, Tax Assessor for the First Taxation Division, Territory of Hawaii, to recover from Ewa Plantation Company the sum of \$20,768.28.

ARGUMENT.

The first point is as to the correctness of the opinion and judgment of the court below on the question of the strike claim settlement (Record, pp. 29-33). This point is covered by assignments of error 1, 2 and 10.

The agreed facts showed, in brief, that in January and February, 1920, the plantation laborers on the Island of Oahu, including those of Ewa Plantation Company, went out on strike, and it became neces-

sary, in order to carry on the plantation, to employ strike breakers and other laborers at large expense; that the Japanese strikers and their families were being maintained by the laborers of that nationality on the islands other than Oahu; that it was decided that the strike should be handled by the Hawaiian Sugar Planters' Association, the membership of which is composed of practically every sugar plantation and mill company in the Territory, the Association agreeing to underwrite the losses of the Oahu plantations, and that all the members should contribute to the expense; it was also agreed that the underwritten losses would be limited to those chargeable to the crops of 1920, 1921 and 1922, and to net losses to other property, such as damage to buildings, etc.; the expense of the strike to the Hawaiian Sugar Planters' Association amounted to $635,959.42, and the losses of the plantation companies on Oahu aggregated the sum of $11,483,357.88; each member of the Association contributed its pro rata of said expense and loss, the share contributed by Ewa Plantation Company amounting to $721,818.95 and said company received from the Association in full settlement of its losses the sum of $2,791,697.72; the last named sum was made up of the estimated losses on the three crops which were in the ground at the time of the strike, as follows: Crop of 1920, $2,324,-931.75; crop of 1921, $133,706.29, and the crop of 1922, $333,059.68; and the contention of the company was, and its tax return was made upon the theory, that the total sum received from the Associa-

tion should not be accounted for as received during the year 1920, but that it should be accounted for in the three years in accordance with the estimated losses on the respective crops of 1920, 1921 and 1922, in other words, that in its tax return for 1921, based on its income for the year 1920, it should account for and include as a receipt only the amount received in connection with the loss to the 1920 crop, to wit, the sum of $2,324,931.75, and account for and include the amounts received in respect of the 1921 and 1922 crops, viz., $133,706.29 and $333,059.68 in the returns of the two following years.

That contention was opposed by counsel for the tax assessor, and the Supreme Court of Hawaii held that the sum received by the company was merely in liquidation of an estimated loss or damage sustained by the company because of the strike, that it could not be apportioned, and that as the whole sum was received in the year 1920 income tax thereon became due in the following year.

The provisions of the Hawaiian statutes which bear on this question are set forth in full in an appendix to this brief.

It may be well for the court to know that while, in these islands, a crop of cane is harvested every year, it takes more than a year, sometimes two years, for a crop to mature. On a large plantation, such as Ewa, there are always three crops in the ground, one newly planted, one about half grown, and one ready for harvesting. It usually takes from seven to ten months each year to harvest a crop of

sugar cane and manufacture sugar therefrom. This will explain why it was that the losses of Ewa Plantation included three crops.

The agreed facts show (Paragraph 3, Record, p. 5) that since 1906 it has been the practice of the sugar companies to make their income tax returns, so far as their income from the sale of sugar is concerned, upon what is called the crop basis, that is to say, instead of deducting from the gross income received during the year the total disbursements made during the same period in respect of all three crops, it has been the custom, so far as the sugar produced was concerned, to deduct the amount expended in the production and marketing of the crop harvested during that year from the proceeds of sale of such crop. The gross income from sugar has been returned on the basis of the current or mature crop, so that all of the receipts from the sale of the sugar of the crop of the taxation period are returned as the income of the taxation period, even though portions of such sugars were actually sold, and the proceeds received either before or after the taxation year, and, similarly, the deductible cost of producing the crop includes all the cost of producing it, notwithstanding that the greater part of that cost was incurred in the preceding two years.

The income tax statute actually requires the doing of that very thing. Section 1307 of the Revised Laws of Hawaii, 1915, provides that "In estimating the gains, profits and income of any person or corporation, there shall be included * * * the amount of

sales of all movable property, less the amount expended in the purchase or production of the same." And the income tax return follows the statute. Schedule "A" includes "(8) Sales of Movable Property" "(b) Sugar" and Schedule "B" includes "(5) Cost of Crop (including property taxes paid)."

In other words when the business of a corporation consists in producing and selling movable property, such as sugar, the taxable income therefrom must be computed by deducting the cost of production from the amount of the sales. That means an accounting on the crop basis.

In the case of the Tax Assessor v. Laupahoehoe Sugar Co., 18 Haw. 206, it appears that the income tax law was amended in 1905 by changing the yearly taxation period so that it should be twelve months preceding January 1, instead of July 1, as theretofore, and one taxation period of six months between July 1, 1905, and January 1, 1906, was provided for. The taxpayers had made their returns on the crop basis, whereas the assessor claimed that the taxable income should be computed by deducting the amounts expended during the year in the production of the several growing crops from the receipts during the year, as had been the previous practice. The action of the tax-payers was sustained. The Court said (p. 208):

"The returns of the taxpayers in these cases are in exact accordance with the statute. Even if, as claimed by the assessor, a portion of the cost of production was incurred prior to the six months' taxa-

tion period and has already been deducted from the income of the taxpayers during the preceding taxation periods, that does not take away the right of the taxpayers to make their returns and compute their incomes as the statute directs."

In the case of In re Income Tax Appeal Cases (Honokaa Sugar Co.), 18 Haw. 596, 599, the question was whether the sum of $6,222.71 expended in 1906 for clearing new land, the crop upon which would be harvested in 1908, should be deducted as an expense incurred in 1906 or as part of the expense of producing the crop of 1908 and not deductible until the latter year. The Court, affirming the decision in the Laupahoehoe Sugar Co. case, held that although the expenditure was made in 1906, it would not be deductible until 1908. Thus the practice of accounting and making returns on the crop basis "in exact accordance with the statute" was thoroughly established and it has been followed ever since.

This case is just the converse of the case last above referred to. There, an expenditure had been made in 1906 which the court held, upon the authority of the Laupahoehoe Sugar Co. case could not be deducted till 1908, when the crop for the benefit of which the expense was incurred would be harvested and sold.

Those two cases lay down the principle that the amounts expended in producing a crop of sugar cane are to be deducted only in the year when the crop is harvested. Until a crop matures and is marketed, the profit thereon, if any, cannot be known. Here

certain moneys have been received in 1920 by way of compensation for extraordinary costs arising by reason of the strike and damage done to the whole of each of two crops (the crops of 1921 and 1922), neither of which would mature and be marketed until after the year 1920. Until each crop had matured and was marketed it could not be known whether there was profit or loss therefrom. It could not be known in the year 1920, therefore, whether the compensation moneys were merely a return of capital or partly a return of capital and partly profit. Upon the principle recognized in the Laupahoehoe Sugar Co. case and upon the authority of that decision, those moneys should not be included in the income tax returns until the crops to which they relate shall be harvested and sold. To hold otherwise would be to ignore the plain language of the statute, reverse the prior decisions of the court, and repudiate a uniform practice of fifteen years' standing.

If everything received in 1920 is to be included in the tax returns of income, the whole system of accounting on the crop basis would be upset and it would be to revert to the method pursued prior to the decision of the Laupahoehoe Sugar Co. case, which the Supreme Court of Hawaii held was wrong. Further, if moneys received in 1920 as compensation for extraordinary costs arising by reason of the strike and damage to the crops of 1921 and 1922 are to be accounted for as income received in 1920, then the amount of loss sustained through the labor strike during the year 1920 must be deducted, be-

cause Section 1308 of the Revised Laws of Hawaii, 1915, as amended by Act 157 Session Laws of 1917, provides that "* * * all losses actually sustained during the taxation period next preceding * * *" shall be deducted.

The practice of determining taxable profits upon the crop basis not only complies with the requirements of the statute, but conforms to accepted accounting principles and is in force in the case of the Federal income tax. An operation by which an asset is acquired or produced does not necessarily result in either profit or loss. It depends upon whether the amount realized upon the sale differs from the cost of acquiring or producing the asset disposed of. If amounts expended in material and labor result in producing a crop of sugar cane, the profit or loss would be the difference between the aggregate amount expended and the amount received for the crop. But until the crop is sold it is impossible to ascertain the profit and taxable income, if any. And so money received on account of compensation for loss sustained on a crop which has not yet been harvested and sold constitutes merely a return or restoration of capital, and hence cannot be considered for income tax purposes until the crop shall have been sold, when it is included in the account and the profit on the crop can be ascertained.

It was impossible to tell in January, 1921, that is, at the time the tax return was required to be filed, what amount would be expended in producing and marketing the crop to be harvested in that year, the

damage to which had been done in 1920. It was not a case of total destruction. The damaged crop was there to be harvested and sold. If the estimation and payment of the amount of damage had been postponed until the crop had been harvested and sold the exact profit or loss could be ascertained and no question would have arisen. But the money representing the estimated loss could just as well be held by the Ewa Plantation Company in abeyance, or in "suspense," as it could have been held for the time being by the Hawaiian Sugar Planters' Association. The transfer of the money by the latter to the company in 1920 did not alter its character or status so as to turn it into a taxable profit of the company in the year 1920. Of course if the 1921 and 1922 crops when harvested and sold without including the compensation had resulted in a profit, the whole of the compensation would be a profit but until the crops were harvested and sold it could not be determined whether or not the compensation or any part of it was a profit.

The money received from the Planters' Association was largely in the nature of reimbursement to the company for extraordinary expenditures incurred in carrying on the plantation and saving the crops by the employment of strike breakers and others. In other words, it was in partial reduction of the cost of keeping the crops alive and assisting them to maturity. But the total actual cost of the crops could not be ascertained, as above pointed out, till they respectively should be harvested and sold.

Referring to the two Hawaiian cases above cited, the Supreme Court of Hawaii said:

"In each of these cases it was held that moneys expended prior to the taxation period in the production of sugar were deductible, not in the period in which the expenditure was made, but at the time the crop was sold. These decisions we think are in accord with the provisions of the statute. In the present case, however, we are confronted with a different set of facts. It must be borne in mind that we are now dealing with a receipt and not an expenditure. * * * Whether this estimate proves to be even approximately correct will necessarily depend upon many contingencies, but irrespective of that feature it is plain to us that the company has not the power merely by an arrangement with the Hawaiian Sugar Planters' Association, or for the sake of harmony in its accounting system or otherwise, to convert a sum received by it as compensation for damages caused by the laborers' strike into an amount expended in the purchase or production of specific growing crops of sugar cane." (Record, p. 32.)

And it should have been equally plain that the tax assessor had not the power "to convert a sum received * * * as compensation for damages caused by the laborers' strike" wholly into a profit upon which the taxpayer should pay income tax. The company had made no attempt to convert the sum it received from the Planters' Association, or any part thereof, into an amount expended in the "purchase or production of specific growing crops of sugar cane." But it did consider that the amounts expended "in the * * * production of specific growing crops of sugar cane" had some place in an income tax account

which charged the tax payer with the compensation received for partial loss of these crops as profit. The compensation awarded had to come into the account either as a part of the proceeds received for, or as a reduction of the expense incurred by it in the production of, the respective crops. Strictly speaking, the money received must be regarded as capital, not income such as profit, until the crop is harvested and the sugar sold, when the profit, if any, can be determined. Neither was the theory upon which the company made its return in 1921 based upon an arrangement with the Planters' Association. The company intended and attempted to make its return for taxation in "exact accordance with the statute" (to use the words of the Court in 18 Haw. 206), consistently with the practice thereunder and in harmony with the decisions of the Supreme Court in which the statute had been interpreted. In order that the crop system of accounting be accurate, it must be consistently carried out, and the reason for deferring charges against a crop apply equally and logically to credits.

Let us attempt to explain the difficulty in the case: the explanation offered is simple, but we believe it to be complete.

It is stated in the syllabus of the court below:

"Where a sum is received by the taxpayers in liquidation of losses or damage sustained because of a laborers' strike income tax *thereon* should be paid for the year in which the payment is made." (Record, p. 26),

and in the decision at page 304:

"but neither the sum involved here nor any part thereof was expended in the purchase or production of movable property and hence *the whole amount thereof is included within 'other * * * income * * ** derived from any source whatsoever during said taxation period'." (Record, p. 33).

The court clearly held that a sum "received * * * in liquidation of losses or damage sustained" is income *of the nature of profits* "and hence the whole amount thereof" is liable for income tax. But surely "a sum received * * * in liquidation of losses or damage sustained" is not income of the nature of profit.

That this is so is clearly shown by Section 1308 of the Revised Laws of Hawaii, 1915, as amended by Act 157, Laws 1917, which give the taxpayer the right to deduct from his income (profits) losses (not compensated by insurance).

The court seems to have proceeded on the theory that where a loss is compensated by insurance, (the loss shall not only not be deducted from the profits, but) the taxpayer shall pay income taxes on the "whole" amount of compensation received by it, as if it were all profit, which is preposterous. The court construed the word "income" as including everything that comes in and therefore concluded that as a receipt is something that comes in, a receipt is income. The word "income" in an income tax law means income of the nature of profit, rents and interest compared to the fruit of a tree, as distinguished from capital, likened to the tree itself.

The definition adopted by the Supreme Court in *Eisner v. Macomber,* 252, U. S. 189, at page 207, was:

> "'Income may be defined as a *gain* derived from capital, from labor, or from both combined', provided it be understood to include profit gained through a sale or conversion of capital assets to which it was applied in the Doyle Case (pp. 183, 185)"

and on page 206 are given illustrations.

What in this case was lost was a part of a crop of sugar cane. The value of the growing crop of sugar cane would usually be in excess of its cost and that excess would represent the profit on the crop, the amount of which would be determined and could only be determined when the crop was harvested and the sugar sold.

Where there was partial loss of a crop, as in this case, the profit, if any, could only be ascertained in this manner. The crop would be harvested and the sugar sold and to the credit side of the account would be added the amount of compensation awarded in respect of the crop and the final balance to the credit of the account would represent the profit upon which income tax would be payable.

As the compensation for the loss on the 1921 and 1922 crops was received, it would be credited to the respective crop and to that extent would reduce the cost of it without affecting the net result.

"Having regard to the very truth of the matter, to substance and not to form," to use the words of the court in *Eisner v. Macomber,* supra, at page 211, it matters not whether the compensation is treated as

part of the receipts or a credit in the account which reduces the cost because the result is the same.

It will thus be seen why the amount of compensation for partial loss of the crops of the years 1921 and 1922 must be assigned to or included in the years in which these crops are harvested and the sugar sold, because unless and until this is done, it is impossible to say what the profit on these crops was.

The case is somewhat analogous to the case of the loss of a ship's freight (in the sense of earnings) compensated by insurance. From the compensation received for loss of freight the shipowner would have to deduct the cost of operating the vessel and the balance, if any, would be income subject to tax. The whole amount received as compensation for loss of freight would not be "net profit or income above actual operating and business expenses" (under Section 1306 Revised Laws of Hawaii 1915) nor "gains, profits and income" (under Section 1307).

Counsel for the tax assessor also referred in the court below to the fact that the amount contributed by the Ewa Company to the Planters' Association had been claimed and allowed as a deduction in the year 1920, claiming that that fact showed that the entire amount received by the company should be accounted for as income for that year. It seems to us, however, that the payment of the assessment and the receipt of the compensation were two separate and distinct things. The assessment was *paid* in a lump sum, while the compensation was carefully

estimated upon and apportioned between the different crops in consideration of the damage done to each. It was not money expended in the production of the crops, but was an expense of the nature of premium for insurance against loss arising through the laborers' strike, properly deductible under Section 1308, Revised Laws of Hawaii, 1915, as amended by Act 157 of the Session Laws of 1917, and would have been payable if no loss had been sustained through the strike and no compensation received. As to the plantation companies on the islands other than Oahu who paid like assessments, the payments were certainly deductible in the year in which they were made, and the fact that the Ewa Company was one of the companies which received compensation does not alter the situation as to it with reference to the payment of the assessment.

The principles herein advocated are recognized by the Federal tax officials under the Federal income tax laws, not only in their practice of accepting tax returns from the Hawaiian sugar plantations made out on the crop basis, but also in the regulations. For instance, Article 38 of Regulations 45 provides, among other things, as follows:

> "If a farmer is engaged in producing crops which take more than a year from the time of planting to the time of gathering and disposing, the income therefrom may be computed upon the crop basis; but in any such cases the entire cost of producing the crop must be taken as a deduction in the year in which the gross income from the crop is realized."

And Article 110 of the same Regulations provides somewhat similarly, among other things, as follows:

"Where a farmer is engaged in producing crops which take more than a year from the time of planting to the process of gathering and disposal, expenses deducted may be determined upon the crop basis, and such deductions must be taken in the year in which the gross income from the crop has been realized."

These rulings are continued in the present regulations (Arts. 38 and 110, Reg. 62).

Consistency is further and more explicitly provided for in Art. 23, Reg. 62, as follows:

"Approved standard methods of accounting will ordinarily be regarded as clearly reflecting income. A method of accounting will not, however, be regarded as clearly reflecting income, unless all items of gross income and all deductions are treated with reasonable consistency."

Thus the Bureau of Internal Revenue recognizes that items of crop income and crop cost should be carried over until the crop is harvested and disposed of, that is, until it is possible to determine the gain from it.

The total amount received by the company represented the damage or loss suffered by it with reference to the three specified crops. The amount received on account of each crop was definitely known inasmuch as the basis for the payment received was the estimated damage to each crop. The amounts received were, therefore, definitely attributable to

the 1920, 1921 and 1922 crops and should be accounted for on the crop basis. In so far as such receipts represented reimbursements for extra crop expenses incurred or to be incurred, the amount received should be treated as an offset to such crop expense and should therefore be accounted for on the same basis and in the same period. In so far as such receipts represented reimbursements for decreased yields, the amounts received might be regarded as advance payments on account of the respective particular crops and should likewise be accounted for on the same basis and in the same period as the expenses attributable to the crops. In so far as it might be contended by the tax assessor that the payments were compensation for damages sustained in 1920 to all three crops it would seem that, if the payments must be returned in that year, corresponding deductions for losses sustained for the same year should be allowed which would offset the credit to income. In other words, if the portions of the indemnity which applied to the 1921 and 1922 crops covered losses sustained on those crops during the year 1920, there would be no taxable profit in respect of these portions because if the indemnity payments received were included in the gross income it would necessarily follow that the losses sustained, which were identical in amount, should be included within the deductions. By attempting to include the 1921 and 1922 crop indemnities in the 1920 income the tax assessor would collect taxes on that much gross income without the company receiving the benefit of

the proper deductions. In a sense the payments were payments by the Planters' Association, through the company, of the extra or additional expenses to which the company was and would be subjected in respect of these crops by reason of the strike and thus diminished the total expense to the company of these crops, so that the payments should be regarded not so much as a source of income to the company as a sharing of the expense by the Association. In a somewhat similar sense the payments might be regarded as in the nature of insurance paid for the losses incurred. After the incurrence of the losses and the receipt of the indemnities the company would stand just where it did before. A cross entry of loss and gain would result the same as no entry at all.

Perhaps a more accurate way of handling the accounts would have been to credit each of the expense accounts with the portion of the indemnity applicable to it, but this would have necessitated a very large number of journal entries and the final result would have been the same. Hence it was deemed better to carry the amounts applicable to the 1921 and 1922 crops in "suspense" until those crops should be harvested and marketed respectively and then to transfer the proper amounts to profit and loss direct.

The principle is that the accounts are kept and the tax returns are made so far as income from the sale of sugar is concerned on a crop basis and that all items, whether receipts or disbursements, which are

definitely referable to a particular crop, should be accounted for on that basis.

We submit that the plaintiff-in-error has the right to insist, and it is all that it is asking with reference to this branch of the case, that the system of accounting upon the crop basis should be consistently applied in this case.

INTEREST ON MAINLAND INVESTMENTS.

The second point is as to the correctness of the opinion and judgment of the court below on the question as to whether interest received by the plaintiff-in-error during the year 1920 on the bonds and notes of mainland railroad and industrial corporations and upon deposits in mainland banks was or was not legally deductible in its tax return of 1921 in ascertaining its taxable income. (Record, pp. 33-48). This point is covered by errors assigned and numbered 3-7, 9 and 10. (Record, pp. 80, 81).

The agreed facts showed:

That ever since the incorporation of Ewa Plantation Company, Castle & Cooke, Limited, a Hawaiian corporation, has been its general agent at Honolulu, and for upwards of twenty years last past Welch & Company, a California corporation, has been the agent at San Francisco of said Castle & Cooke, Limited; that at all times during said period the sugar produced by the Ewa Plantation Company has been sold on the mainland of the United States and the proceeds of sale have been received by Welch & Com-

pany and deposited by it in California banks, and credited on its books to Castle & Cooke, Limited, for account of Ewa Plantation Company; that against said credit the Ewa Plantation Company has drawn, from time to time as needed, moneys required by it for the payment of expenses of its plantation and dividends upon its stock; that bonds and notes of foreign (mainland) railroad and industrial corporations were purchased by Welch & Company with the surplus moneys of the Ewa Plantation Company so held as aforesaid by the former Company and the said bonds and notes thereafter, until they were sold on the mainland, remained on deposit with said Welch & Company and none of said bonds and notes, or the proceeds with which they were purchased, have been held in said Territory, nor have they been physically present therein at any time;

That the Ewa Plantation Company after including it in Schedule A of its return deducted the interest accruing to it from these investments during the year 1920 in its Territorial income tax return of 1921, by including it in Schedule B (Record, pp. 16, 18), and that the Territory, acting through its tax assessor, disallowed such deduction; and

That at no time heretofore has the Territory considered income derived from such investments as taxable income or included such in assessing the incomes of corporations or individuals under the laws of the Territory. The issue raised is: Is interest accruing from such bonds, notes and bank deposits

properly deductible prior to arriving at taxable net income under the Territorial Income Tax Act?

A. The Territorial Income Tax Act has been in force since July 1, 1901. It was originally Act 20 of the Session Laws of 1901. It was incorporated in the Revised Laws of 1905 as Chapter 99 and is now Chapter 94 of the Revised Laws of 1915, minor amendments (e. g. as to amount of exemption and the taxation period), which have no bearing on the present question, were made in 1905 and 1909. Prior to 1901 Hawaii had an income tax law—Act 65, Session Laws of 1896—in which identically the same language was used in Sections 1 and 2 thereof to define the income subject to taxation; this act was however declared unconstitutional in 1897, (*Campbell v. Shaw,* 11 Haw. 112.)

By all these acts the taxable income of corporations is and was specifically limited to that derived from "property owned and every business, trade, employment or vocation carried on in the Territory," and in this respect corporations, foreign and domestic, were placed on the same plane as resident and non-resident individuals.

Section 1306 of said Chapter 94 (Sec. 2, Act 20, Session Laws of 1901) provides that in the case of *corporations* income tax shall be levied:

"On the net profit or income above actual operating and business expenses derived * * * from all property owned, and every business, trade, employment or vocation, carried on in the Territory of Hawaii, of all corporations, doing business for profit in

the Territory, no matter where created and organized."

and Section 1305 of Chapter 94 (Sec. 1, Act 20, Session Laws 1901) provides that in the case of *individuals* income tax shall be levied:

"Upon the gains, profits and income over and above Fifteen Hundred Dollars derived by *every person* residing in the Territory of Hawaii, from all property owned, and every business, trade, profession, employment or vocation, carried on in the Territory, and by *every person residing without* the Territory from all property owned, and every business, trade, profession, employment or vocation carried on in the Territory."

The Act thus makes the rule in the Territory the same both as to persons, whether resident or non-resident, and as to corporations, whether domestic or foreign; the taxable income is only that part which is derived "from property owned or business, etc., carried on in the Territory." This is exceptional. As a general rule income tax laws impose the tax upon income of residents (whether individuals or corporations, citizens or aliens) *from whatever source derived* whether from within or without the taxing jurisdiction, but only upon that part of the income of non-residents (at least unless they are citizens) which is derived from sources within the jurisdiction. Such is the case under the Federal Income Tax Act of 1918 and prior statutes, under English statutes, and under the laws of most of the States which tax income. (Black on Income

Taxes, 2nd Ed., Chapter 9, Section 252). Some States, as for instance, Wisconsin, (see appendix Black pages 643 et seq) make a distinction between foreign investments and foreign business in this respect, by including in the taxable income of residents from foreign sources only that received from foreign investments, and excluding that received from foreign business. The Territory goes still further in this direction by excluding from the taxable income of residents not only income from foreign business, but also, we claim, income from foreign investments. Black, (pp. 351, 352) regarding such income in Hawaii as non-taxable, speaks of this exclusion as being exceptional, using the following language:

"It is also within the competence of the several States to tax their resident citizens upon intangible personal property, consisting, for example, of shares of stock in foreign corporations, and no constitutional provision is thereby violated. Naturally, therefore, they also have the power to tax income derived from such sources and this has generally been provided for in the income tax laws of the States. In Hawaii, it is true, the taxes are levied on 'income derived by every person residing in the Territory of Hawaii from all property owned, and all business, trade, profession, employment or vocation carried on in the Territory.' *But this is exceptional.*"

B. The income in question was not received "from any business, trade, employment or vocation carried on in Hawaii and therefore the statute (R. L. Sec. 1306) may be regarded as though it read: "There

shall be levied a tax on the income from all property owned in Hawaii." The question then briefly stated is, are the bonds, notes and bank deposits referred to in the Submission "property owned in Hawaii?" There is no doubt that they are property belonging to plaintiff-in-error. The expression "owned in" is frequently used in either one of two senses, either as referring to the fact that the *owner* is in the place mentioned or as referring to the fact that the *property* owned is in the place mentioned. R. L., 1915, Sec. 1305, contains a provision similar to that of Sec. 1306, but with reference to the income of *persons,* and taxes the income of persons in Hawaii as well as those residing without the Territory, describing in both instances, in identically the same language as above quoted, the property from which the income is derived. This we claim clearly indicates that the expression "owned" was not used in Section 1305 in the sense of the *owner* being in Hawaii because that Section recognizes that non-residents also can own property *in* Hawaii. The same meaning must be given to the expression "owned in" when used in Section 1306, and it must be taken as referring to the property and not to the owner; and the final form of the question is, are these bonds, notes and bank deposits *"property in Hawaii?"* It was conceded in the court below by the defendant-in-error that the case stands as though the statute read: "Income from property in Hawaii owned by the taxpayer." (See Record, pp. 37, 38.) The court below expressed itself as not being as ready as counsel for

the Territory to accept this construction of the meaning of the statute and stated that it could be strongly argued that the expression "property owned in Hawaii" has reference to the place of ownership and not to the location of the property. It said (Record, p. 38) that while it might be true that if a person were asked "What property do you own in the Territory" he would not in answer enumerate bonds and notes of foreign or mainland corporations or deposits in foreign or mainland banks; on the other hand, if the San Francisco agents were asked in reference to the property in question, "Where are these bonds, notes or bank credits owned," the answer obviously would be "In the Territory of Hawaii," and that answer would be entirely correct. The court below overlooked the fact that if the expression has reference to the place of ownership and not to the location of the property the income of non-residents would escape taxation in Hawaii, the place of ownership in such cases being elsewhere than in Hawaii; the income of the property of a non-resident could in no case be taxed, while that of a resident would never be exempt in whatever part of the world it might be situated.

The fact, also that by Sec. 1306, supra, corporations, domestic and foreign—"corporations * * * *no matter where created and organized*"—are placed for income taxation purposes on the same plane seems to us conclusive upon the question that the statute subjects to taxation the income of property actually situated in Hawaii and not the income of

property the ownership of which was in Hawaii, for if the latter were the meaning of the language used in the statute the income of property in Hawaii owned by a foreign corporation would escape taxation.

That the income of non-residents and foreign corporations derived from property in the Territory should be exempt from taxation was not the intention of the legislature. Its intent gathered from the ordinary meaning of the language it used in reference to all classes, was to tax income derived from all property and business in the Territory, whether such property or business was owned or carried on by corporations or individuals, resident or non-resident.

The power of the legislature as to non-residents extended no further than the taxation of the income of property actually within the Territory.

> Gray's Limitation of Taxing Power and Public Indebtedness, Sec. 71;
>
> *Dewey vs. De Moines,* 173 U. S. 193.

It is conceded by the plaintiff-in-error that the legislative power in respect to the taxation of residents (individuals and corporations) is absolute and unlimited, (Gray, (supra) Sect. 44) and that the Legislature could, by the use of appropriate language, *exercise* this power so as to subject to taxation income derived from all sources whether within or without the Territory. What the plaintiff-in-error claims is that the language used by the Legislature of Hawaii shows that it did not intend to exercise

to its fullest extent the power it possessed in the case of corporations and residents, but limited and confined the exercise of that power to the taxation only of income derived from property within the Territory.

The extent of its powers,—limited as to non-residents, unlimited as to residents,—must be presumed to have been known by the legislature. Knowing its powers, it must be presumed from its use of the same language in describing the taxable income of corporations, residents and non-residents to have intended that the meaning of the language used should be the same whenever used:

Rhodes vs. Weldy, 45 Ohio St., 242; 15 Am. St., Rep. 584, 591-592;

Endlich, Interpretation of Stats. Secs. 382, 387; 26 Am. & Eng. Ency of Law, p. 610.

and that, whatever the property was the income of which it proposed to tax, all should be on the same basis, namely: the income from all property and business actually within the Territory should be taxed wherever the owner might reside.

It being incontrovertible that the only income of non-residents which could be taxed is that derived from property or business actually situated or conducted within the Territory, it follows that the legislative definition of taxable income must refer when used in respect to residents (individuals or corporations) to the actual situs of the property or the business. If the intention had been different it cannot be doubted that different language would have been

used. It would have been so easy and so natural to have declared that income from all property, where-ever situated, owned by individuals or corporations, was taxable, that such a declaration would undoubtedly have been made in the statute if that had beer the intent of the legislature.

In De Ganay v. Lederer, 239 Fed. 571 (referred tc at length hereafter) where the court held that language almost identical with that of the Hawaiian statute referred to the *physical location* and not the *ownership* of property, the court said:

"When we find words which have a well known and universal use, and which, if so read, express a meaning which Congress at least may have intended, we are justified in assuming that they were so used, and not justified in giving them a strange and before unheard of meaning, in order to force a construction which, if that meaning was in fact intended by Congress, might have been expressed in other and apt words."

C. Comparison with other legislation: When other states have undertaken to tax income from property outside their Territorial limits, they have done so by appropriate language. Thus, in South Carolina, the taxable income of residents is that received from certain enumerated kinds of property, and "from any other source whatever," while the words used to describe the taxable income of non-residents are identical with those used as to all classes in the Hawaiian statute. In North Carolina, the statute includes income from "any and all

sources." In Virginia the language of the statute is "all rents, * * * interest upon notes, bonds, or other evidences of debt, of whatever description of the United States, or any state or county, or any corporation * * * and all other gains and profits derived from any source whatever." In Winconsin residents are taxed upon "all income * * * derived from sources within or without the State," while non-residents are taxable only in respect to income "derived from property within the State or within its jurisdiction." (Black, supra, pp. 643 et seq.)

Under the Federal Income Tax Act of 1918, Section 212, persons residing within the United States are taxed upon the "income derived from any source whatever," non-residents under Section 213 being taxed only in respect of "income from sources within the United States." The same distinction is made in the earlier Federal Acts. It must be assumed that the Legislature of Hawaii, before passing the Income Tax Act of 1896, had made a study of similar legislation in other countries. Black, supra, Section 194, page 230, says that: "A comprehensive statute, modelled on the various acts of Congress, was passed by the Territory of Hawaii in 1901." The earlier Act of 1896 had evidently escaped the author's attention. The actual facts are thus stated by the Supreme Court of Hawaii in Robertson vs. Pratt, 13 Haw. 590, at 591:

"The statute" (that of 1901 now in question) "was taken largely from that of 1896, which was taken largely from that passed by Congress in 1894, which

in turn was taken largely from those passed by Congress during the years 1861-1870."
That case held the Act constitutional, as did also the Circuit Court of Appeals for the Ninth Circuit in W. C. Peacock v. Pratt, 121 Fed. 772. The Act of 1896 having been framed after a study of the acts of Congress, it is of interest to note the language of the Federal Act of 1894. Under that Act citizens and residents were taxed upon the income derived "from any kind of property, rents, interest, dividends * * * or from any profession, trade, * * * carried on in the United States or elsewhere, or from any other source whatever," while non-residents were taxed only upon "income from all property owned and of every business, trade and/or profession carried on in the United States."

The fact that, with this act before it, the Legislature of Hawaii in 1896 and all subsequent legislation, rejected the all-embracing description of income taxable to residents and adopted in identical language only that applicable to non-residents, would seem to us conclusive upon the proposition that the intention of the Legislature of Hawaii was to limit the exercise of its power of taxation to the income of property actually within its territorial limits.

D. Mobilia sequuntur personam. It being conceded (Record, pp. 37, 38) that the case stands as though the statute read "income from property in Hawaii owned by the taxpayer," and that the bonds, notes and deposits in question have never been physically present in the Territory, the income therefrom

can be taxable only if, by the introduction of the legal fiction *mobilia sequuntur personam*, they can be said to have a situs in Hawaii.

1. It is an elementary rule of statutory construction (embodied in Hawaiian law as Section 9, Revised Laws of Hawaii, 1915) that:

"The words of a law are generally to be understood in their most known and usual signification, without attending so much to the literal and strictly grammatical construction of the words as to their general or popular use or meaning."

The popular and general meaning of the language of the statute leaves no room for the introduction of any legal fiction; the legislature was not enunciating any such fiction, but in speaking of property within the Territory was speaking in plain words and to the plain understanding of men in general. The person of ordinary understanding certainly would interpret the language as meaning property actually in Hawaii, and would not understand it to include also property which, while not physically in Hawaii, was given a situs there by virtue of a legal fiction.

2. A rule of construction of taxation statutes is:

A statute imposing taxes is to be strictly construed against the government and in favor of the taxpayer; that no person and no property is to be included within its scope unless explicitly placed there by the clear language of the statute, and no heavier burdens imposed than the plain meaning of

its terms will warrant; that the intention of the taxing power must be expressed in clear and unambiguous language and that any fair doubt as to the construction of an act imposing taxation should be resolved in favor of those upon whom the burden is sought to be laid.

See *Black* (supra) Sec. 217;
Gould v. Gould, 245 U. S. 151, followed in Haiku Sugar Co. v. Johnstone, 249 Fed. 103, 109 (Ninth Circuit), and in
Frear v. Wilder, 25 Haw. 603, 607;
U. S. v. Goldenberg, 168 U. S. 95, 102, 103;
Eidman v. Martinez, 184 U. S. 578;
U. S. v. Isham, 17 Wall. 496, 504;
Benziger v. U. S., 192 U. S., 38, 55;
Spreckels Sugar Ref. Co. v. McClain, 192 U. S. 397, 416;
Parkview Bldg. & Loan Assn. v. Herold, 203 Fed. 896;

See also *Penn. Steel Co. v. New York City,* 198 Fed. 774, where in construing the federal corporation tax law of 1909 the court said:

"This statute levying as it does a tax upon the citizen, must be strictly construed; it can't be enlarged by construction to cover matters not clearly within its import. The question is not what Congress might have done or should have done, but what it actually did do. When this is ascertained, the duty of the court is accomplished."

Applying these principles to the question in issue, we submit that if in the income tax statute there is

any ambiguity as to what the legislature intended should be covered by the language "property owned in the Territory"—as to whether it covered not only property actually in Hawaii, but also property which under a legal fiction might have a situs there, or as to whether any particular fund or kind or class of gain or acquisition constitutes taxable income within the meaning of the law—then the substantial and reasonable doubt arising must be resolved in favor of the taxpayer and not in favor of the government.

There are two other rules of statutory construction that should be applied in ascertaining the intention of the Legislature.

(a) Statutes in *pari materia* are to be read and construed together.

Under this rule of construction there should be considered, in connection with the income tax act, Sec. 6 of Chapter 3, R. L. 1915, entitled "Operation of Laws" and reading as follows:

> "The laws are obligatory upon all persons, and all persons are subject thereto, whether citizens of this Territory or citizens or subjects of any foreign state * * * while within the limits of this Territory * * *. The property of all such persons, while such property is within the territorial jurisdiction of this Territory, is also subject to the laws."

The term "territorial jurisdiction" has reference to actual boundaries and locality. Thus "a tract of land or district within which a judge or magistrate has jurisdiction is called his territory and his power

in relation to his territory is called his territorial jurisdiction."

Words and Phrases, Vol. 8, page 6925.

Robinson vs. City of Norfolk, 60 S. E. 762.

Taking these two statutes together, the expression "property owned in the Territory" used in the income tax act, must mean property actually located within the territorial limits of the Territory.

(b) Contemporaneous Construction. What the intention of the Legislature appeared to be to the executive branch of the government of the Territory is shown also by the construction put upon the act by those charged with the duty of administering and applying it. Income tax legislation has been in force in Hawaii for a period of over twenty-one years. Throughout this period the language defining what is taxable income has always remained the same, and the agreed facts (Record, p. 8) show that at no time heretofore has the assessor or any of his predecessors considered income derived from investments such as are now under consideration, taxable income or included such in assessing the income of corporations or individuals.

The construction therefore placed upon the acts by the administrative officers for over twenty-one years has been that the language of the legislature did not extend to or cover such income, and that the legislature did not intend that the same should be taxable.

To the effect that this practical construction is entitled to great weight and the most respectful con-

sideration, and should not be overruled without cogent reasons, see

Black (supra) Sec. 220;

U. S. v. Recorder, 1 Blatchf. 218; Fed. Cas. No. 16129;

Shell's Executors v. Fauche, 138 U. S. 572;

Heath v. Wallace, 138 U. S. 582;

Pennoyer vs. McConnaughy, 140 U. S. 23, in which case it was held that:

"The principle that the contemporaneous construction of a statute by the executive officers of the government, whose duty it is to execute it, is entitled to great respect, and should ordinarily control the construction by the courts, is so firmly embedded in our jurisprudence that no authorities need be cited to support it."

The principle is thoroughly established in Hawaii as to tax statutes as well as other statutes.

County of Hawaii v. Auditor, 25 Haw. 372, at p. 377.

E. The common law maxim *mobilia sequuntur personam* has, in its application to taxation matters, never been recognized or adopted as law in Hawaii.

In 1892 the common law of England as ascertained by English and American decisions was by statute (C. 57 Session Laws of 1892, Sec. 5; now Sec. 1, R. L. 1915) declared to be the common law of Hawaii *"except as provided * * * or fixed by Hawaiian judicial precedent";* this statute went into effect on January 1, 1893.

The maxim above referred to did not in 1893 become part of the law of Hawaii for the reason that,

as will presently appear, that part of the common law had previously been rejected by the courts of Hawaii.

Prior to that year the courts were by various statutes authorized to decide causes according to reason and equity, and to adopt the principles of the common law when and only insofar as they considered them founded in justice and not contrary to Hawaiian law and usage. See Section IV, p. 5, Laws of 1847 and Sections 14, C. 3 and 823, C. 12, Civil Code 1859, reading as follows:

"The reasonings and analogies of the common law, and of the civil law, may in like manner be cited and adopted by any such court, so far as they are deemed to be founded in justice, and not at conflict with the laws and usages of this kingdom. The principles sustained by said courts when sanctioned by the supreme court, shall become incorporated with the common law of the Hawaiian Islands, and shall form an essential ingredient in the civil code: Provided always, that the legislative Council of Nobles and Representatives, may by act sanctioned by His Majesty, and duly promulgated, correct, alter, or abrogate the principles of such abstract judgments and decisions, in analagous cases afterwards to arise before said courts, or any of them."

Section 14 Civil Code 1859: "The judges have equitable as well as legal jurisdiction, and in all civil matters, where there is no express law, they are bound to proceed and decide according to equity, applying necessary remedies to evils that are not specifically contemplated by law, and conserving the cause of morals and good conscience. To decide equitably, an appeal is to be made to natural law and reason, or to receive usage, and resort may also be had to the laws and usages of other countries."

Section 823 Civil Code 1859: "The several courts may cite and adopt the reasonings and principles of the admiralty, maritime, and common law of other countries, and also of the Roman or civil law, *so far as the same may be founded in justice,* and not in conflict with the laws and customs of this kingdom."

While the courts usually followed the common law of England, they rejected it in many important particulars. Some of the principal cases in which the common law was rejected are the following: *Wood v. Ladd* (1847), 1 Haw. 23, holding a seal not essential to mortgage; *Campbell v. Manu* (1882), 4 Haw. 459, holding seal not essential to deed; In *Re F. R. Vida* (1852), 1 Haw. 107, holding widow entitled to dower in leasehold estate; *Awa v. Horner* (1886), 5 Haw. 543, holding conveyance to two or more creates tenancy in common, not joint tenancy; *Kake v. Horton* (1860), 2 Haw. 209, holding action maintainable for damages for death by wrongful act; *Thurston v. Allen* (1891), 8 Haw. 392, holding rule in Shelley's Case not law in Hawaii. In the case last cited the Court said (pp. 398, 399):

"We and our predecessors on this bench have felt free to examine into the reasoning of every principle of the common law as it has been presented to us for adoption from time to time * * * when we have followed and adopted the common law, we have felt that its reasoning was sound and just and its principles adapted to our circumstances. When we have felt otherwise we have not hesitated to reject it * * *. They (the precedents and principles laid down by the courts of those countries where the common law prevails) are not absolutely authoritative, and until

further restrained by statute, we shall continue to rejoice in our freedom."

Being thus at liberty to adopt or reject the maxim *mobilia sequuntur personam,* the Supreme Court of Hawaii in the year 1871 in the case of Hackfeld & Co. v. Minister of Finance, 3 Haw. 292, and later in 1879, in the case of Hackfeld & Co. v. Luce, Tax Collector, 4 Haw. 172, rejected it, and emphatically declared: That it was not the law in Hawaii; that the advantage resulting from taxation legitimately belongs only to the government giving protection to property; that in the adjustment of systems of taxation it has been very generally rejected elsewhere on the ground that it was productive of unjust consequences, and that the legal fiction could not become law except by legislative enactment.

In *Hackfeld & Co. v. Minister of Finance,* 3 Haw. 292, the Court said (p. 294):

"The question for our decision is, whether the laws of this Kingdom authorize the assessment of taxes on personal property situated in a foreign country, although the owner resides here."

In that case the property sought to be taxed belonged to the plaintiff, a domestic partnership, and consisted of both tangible and intangible personalty —"money and goods"—at the time of assessment in Europe and the United States, included therein being consignments of merchandise in San Francisco and elsewhere in the United States. The statute under which the question arose defined personal

property as "all personal property of whatever kind * * * and every species of property not included in real estate." The assessment could be sustained only by invoking the doctrine of the maxim *mobilia sequuntur personam.* The court held that no portion of the property was taxable, criticising the maxim as a legal *fiction,* and declaring that it could not become *fact,* as applicable to taxation, except by legislative enactment. The repudiation of the maxim was complete; if it had been adopted the money and goods in question could have had no other situs than Hawaii, where the owner resided, and would therefore have been taxable.

The language of the court is in part as follows:

"It is said personal property, by a fiction of law, has no situs, except with the owner. It is always supposed to be with him, wherever he may reside.

"Mr. Justice Story, Conflict of Laws, Sec. 550, says that a nation, in whose territory any personal property is actually situated, has an entire dominion over it while therein, in point of sovereignty and jurisdiction, as it has on immovable property situated therein.

"Property should pay taxes to the government which protects it, and *the legal fiction which makes the situs of personal property wherever the owner is,* with all the unjust consequences which would follow, *cannot become a fact, as applicable to taxation, except by legislative enactment."*

The court cited with approval the highly instructive case of Hoyt v. the Commissioner of Taxes, (1861) 23 New York Reports, 224, in which it is said (p. 228) "There seems to be no place for the fiction of which we are speaking in a well ordered system of taxation," and then continued:

"Upon principle, it is the legitimate right of the government which gives *protection to property,* to have the advantage resulting from taxation.

"There is no more reason why this property should be taxed here, than the property situated here should be taxed at the residence of the senior partner in Europe. *To impose a tax upon property thus situated, requires a legislative enactment, distinct and clear in its terms.*"

Hartwell J., in a concurring opinion quoted in support of the decision Section 6 of the Civil Code of 1859 which limits the effect and operation of laws to property "within the territorial jurisdiction of this Kingdom." This section is still in force as Section 6, Chapter 3, R. L. 1915.

In Hoyt v. Commissioner of Taxes (supra) decided in 1861, the decision was expressly limited to the case of visible and tangible property, the court saying however that "it may be that capital thus situated" (invested abroad) "should be regarded as foreign and not domestic in the absence of any special statutory provision in that regard." Later, in the case of People v. Gardner, 51 Barb. (N. Y.) (1868) 353, it was held that the maxim was equally inapplicable to *intangible* property, and this case, as will hereafter appear, was in great measure the basis of the decision in Hackfeld & Co. v. Luce, Tax Collector, 4 Haw. 172.

In People v. Gardner, great stress was laid by counsel for the assessor upon the word "owned" in the expression "owned in the State," used in the statute, but it was held "that the fact that property

was owned by the relator was not alone sufficient to justify the action of the assessors. To produce that result, the additional circumstance was equally essential, that the property should be within the State." (Id. 356, 357). Counsel for the assessor urged upon the consideration of the court that as the property consisted of what the law denominates choses in action, being obligations of a tangible nature it was within the state because the relator was its owner. But the court again held that the legal fiction that personal estate follows its owner had no place in a well ordered system of taxation. It said:

"As to visible and tangible property capable of having an actual situs this fiction has not been allowed to prevail, so as to render such property liable to taxation when it was not within this state (People vs. Commissioner of Taxes, 23 N. Y. 224), and the reasoning of the Judge through which that conclusion was reached, is equally applicable to the present case though it was not intended to be applied to a case of this description. Upon that subject Judge Comstock remarked: 'This conclusion is intended to embrace only property which is visible and tangible so as to be capable of a situs away from the owner or his domicil; and I do not consider the question in reference to personal estate of a different description. It must be within this state in order to be subject to taxation, for so is the statute; but that may be true of choses in action, and obligations for the payment of money due to a creditor resident here from a debtor whose domicil is in another state. If the securities are separated from the person and domicile of the owner, and are actually in the hands of an agent in another state for collection, investment and re-investment there, it may be that capital thus situated should be regarded as foreign and not

domestic, in the absence of any special statutory provision for such a case (Id. 240).' That it should be so regarded results, necessarily in the theory of taxation previously considered from the circumstance that the right to tax is derived from the protection afforded by the laws to the property taxed, and that theory is maintained by this decision as the true source from whence the right of taxation is legally as well as logically secured."

In *Hackfeld & Co. v. Luce,* Tax Collector, (1879) 4 Haw. 172, the Court having declared (p. 177) that the property of a non-resident could not be taxed "unless it has an *actual situs* within the jurisdiction," and also that "it is quite competent for any government to provide that any tangible personal property situated within its jurisdiction may be taxed there irrespective of the residence of the owner," stated that the questions involved were:

"Whether the *notes and securities* which the plaintiffs allege are in their possession, as agents of persons residing in foreign countries, *are property; and if they are property whether they have a situs within this country.*"

It answered both questions in the affirmative and in its decision cited with approval People v. Gardner (supra). After stating the question in that case, which was—whether capital invested in Wisconsin and Illinois, for which securities were taken and held in those states by the relator's agents, were liable to taxation in New York, it said: The argument set forth in the opinion of the court is so applicable to this case that we quote from it largely:

"It is clear that the property on account of which the assessment is made, had no actual location or situs within this State (New York). For the moneys loaned and the securities taken and held for the payment of such loans were actually in the States of Wisconsin and Illinois. *So far as they were things having a substantial existence, they were in those States AND NOT ELSEWHERE.*"

It then proceeded with its own decision as follows:

"Applying that to the case before us, the property in question has *no situs* in Germany where the persons reside for whose benefit the securities are held, but so far as they have a substantial existence anywhere, they are in this country. We continue the quotation:

"The validity of the agreements, under which the loans were made, the protection of the securities taken for their payment and the remedies provided for enforcing the securities *depend* alike *upon their laws;* and in no respect do the persons for whose benefit the securities are holden derive any benefit from the laws of the country in which he resides. * * * Again the Court says:

"*By a legal fiction, the personal estate of the owner has for some purpose been deemed to follow its owner, but in the adjustment of systems of taxation, this fiction has been very generally rejected on the ground that it was productive of unjust consequences.* And other cases exist where, for a like reason, its application has been denied. As to visible and tangible personal property capable of having a *situs* away from the owner or its domicile, this fiction has not been allowed to prevail. * * * When the securities are separated from the person and domicile of the owner, and are actually in the hands of an agent in another State, for collection, they must be regarded as being in the State where the securities are." (Hoyt v. Commissioner of Taxes, 23 N. Y. 224).

These Hawaiian cases have never been reversed and still stand as the law of the Territory. They decide that the situs of personal property, both tangible, e. g. goods and merchandise, and intangible, e. g. moneys (credits), notes and securities, have their situs for purposes of taxation where they are actually situated *and not elsewhere;* and that it cannot in one case be taxed or, in the other, escape from taxation by the introduction of a legal fiction which has no place in a well adjusted system of taxation.

In considering these Hawaiian cases it must be remembered that it is of no moment whether they, and the decisions in New York and other states cited in them, are or are not in harmony with the weight of authority elsewhere—the only question being as to whether or not they repudiated, in regard to taxation matters, the common law maxim above referred to.

We are at a loss to understand how, in view of what the Supreme Court of Hawaii *said* in those cases, the court below could arrive at the conclusion (Record, p. 47) that the court "*merely intended to hold* that the maxim is not of universal application and may yield to the exigencies of particular circumstances."

In another case, Estate of Hall, 19 Haw. 531 (1909) it was held that shares of stock in a domestic corporation owned by a non-resident were for inheritance tax purposes, property *within* the Territory. It may be argued that the decision on that

point was obiter as the statute taxed all personal property "within or without the Territory" but the fact remains that the question as stated by the court (p. 532) was "Whether the shares referred to are property within this Territory," and if the maxim under discussion had been in force the shares would have been property in New Jersey where the testatrix was domiciled and not in Hawaii. The decision indicates that in the court's opinion, following its earlier decisions, the maxim was not in force.

The legislature is always presumed to know what is the existing state of the law whenever any statute is passed.

"As it is the function of the Legislature to express the national will by means of statutes, it is essential that the Legislature should know what is the existing state of the law whenever any statute is passed, and it is always presumed that the Legislature possesses such knowledge."

Endlich Interpretation of Statutes, Sec. 182, p. 251.

The maxim having no place in Hawaiian law as applied to taxation, it is obvious that the legislature, in placing a tax upon income derived from property in Hawaii, could neither in 1896, when the first income tax act was passed, or at any time subsequent, have intended to tax income derived from property which could have no situs for that purpose in Hawaii, except by virtue of a legal fiction which, as far as the Territory was concerned, did not exist.

G. Even if it should be held that the common law maxim *mobilia sequuntur personam* has not been repudiated by the Courts of Hawaii, so far as regards matters of taxation, the plaintiff-in-error claims that under the circumstances shown in the agreed facts, the bonds, notes and deposits have acquired a *business situs* on the mainland; that by reason of that fact, they are not "property in the Territory," and hence the income therefrom is not taxable under the present statute.

In the earlier period of the common law movable or personal property was mostly tangible and consisted largely of gold, silver and jewelry which were carried on the person, and horses, cattle and other animals which accompanied the person. Hence originated the legal fiction, expressed in the maxim, that personal property followed the person and had its situs where, and only where, its owner was. With the growth of industry and commerce, however, and the consequent increase in the volume and kinds of personal property, it became more and more a matter of practical necessity or convenience to apply the doctrine that legal fictions must yield to facts when justice so required.

A series of cases, commencing, we believe, with Catlin v. Hull, 21 Vt. 152, show a gradual judicial development in the course of which in taxation matters the fiction embodied in the maxim has lost much of its ancient force and has come to be honored more, if anything, in its breach than in its observance, and,

as said in Commissioners vs. Leonard, 27 Kans. 531, "it is subject to so many limitations and exceptions that it is quite as liable to mislead as to furnish a correct guide when considered alone."

It first came to be recognized that, at least, tangible personal property could be severed by law from the person of its owner and dealt with as having its situs, for purposes of taxation, and for various other purposes, where it actually was, even though its owner might be domiciled in another jurisdiction and even though the property might be regarded as also having a situs in such other jurisdiction for similar purposes. In other words, the property might have a situs and be taxed in each of two jurisdictions. Now, however, the law as to tangible personal property in this respect has evolved further still. It has, indeed, passed beyond the stage of statutory law to that of constitutional law, and now the taxability of tangible personal property, when it is permanently located in a jurisdiction other than that of its owner, not only is not confined to the jurisdiction of its owner, but *does not even exist* as to that jurisdiction.

See *United States v. Bennett,* 232 U. S. 299;
Union Refrigerator Transit Co. v. Kentucky, 199 U. S. 194;
Delaware L. & W. R. Co. v. Pennsylvania, 198 U. S. 341;
So. Pac. Co. v. Kentucky, 222 U. S. 63, 74.

On the other hand, if the property is merely casually in a jurisdiction other than that of its owner, or

merely in transitu, it can be taxed only in the jurisdiction of its owner, because it has no other situs or domicile.

A similar course of evolution has been going on in the case of *intangible* personal property, although naturally it has not been going on so long and has not yet gone so far, inasmuch as intangible personal property (bonds, stocks, notes, accounts receivable, etc.) came into its modern position of importance later than tangible personal property.

As the law now stands, such property *may, in general,* be taxed at the domicile of the owner, but it does not follow that it may be taxed at the domicile of the owner in *all* cases; or that, in cases in which it might otherwise be taxed, it comes within the meaning of the particular statute in question; there may or may not be the *power* to tax, and there may or may not be the *intention* to tax. The doctrine that no question of physical situs arises in the cases of intangible property because it is not physical, and hence that its situs must be where its owner is because it can be nowhere else, has been in great measure discarded. It is now usually held that, at least under many circumstances, bonds, notes and credits which have assumed what may be called a concrete form,—i. e. are evidenced in a manner which gives the evidence some physical character of property,—are in themselves property, and not the mere evidences of debt, and that as such they may by law be severed from the person of their owner, and when so

severed, they have a situs and may be taxed where they are, even though they are in a jurisdiction other than that of their owner.

The severance which effects such a result occurs when they are used in or connected with business carried on in the place where they are physically located, or are in the custody of an agent there, who has more or less control over them, as for instance, the power to sell and reinvest the proceeds or otherwise deal with them, and the situs they thus acquire is called their *business situs.* From an examination of the authorities, which adhere to the general rule that personalty for purposes of taxation follows the person of its owner, it will be found that they usually have in mind cases, (a) in which the certificates of stock, notes, bonds, etc., are in fact at the location of the owner, or, if elsewhere, that they are elsewhere only casually, or by reason of passage in transitu or merely temporarily for the purpose of evading taxes or otherwise, and have not there acquired a business situs, or (b) where the question is not of the *intention* but of the *power* to tax. In such cases courts even still often speak of a bond, certificate of stock, etc., as mere evidence of a debt, and of the debt itself as the property, which, of course, is the property of the creditor and not of the debtor, and so apparently must have its situs where the creditor is. In examining the authorities, the particular facts in each case must be considered; it is not enough merely to get as far as the general rule.

As to what constitutes "business situs" see:

Johnson County vs. Hewitt, (Kan.) 14 L.R.A. (NS) 493;

"It is not necessary to determine precisely what facts will be sufficient in either case to establish the independent business situs for notes and mortgages, but, generally, the element of separation from the domicile of the owner, and fairly permanent attachment to some foreign locality should appear, together with some business use of them, or some power of managing, controlling, or dealing with them in a business way."

That the taxable situs of notes, bonds, mortgages and the like, being in themselves property, is, in the absence of express statutory direction, the place where they are found, and not the domicile of their owner, see Wilcox vs. Ellis, 14 Kan. 588, in which the power of the state to tax a citizen and resident of Kansas on money due him in Illinois evidenced by a note, was denied.

Fisher vs. Commissioner of Rush County, 19 Kan. 414;

Blain vs. Irby, 25 Kan. 499;

People vs. Gardner, 51 Barb. 352;

People ex rel Jefferson vs. Smith, 88 New York, 576;

Poppleton vs. Yanhill, 18 Or. 377;

Commonwealth vs. West India Oil Refining Co. (Ky.) 129 S. W. 301;

Commonwealth vs. Avery, (Ky.) 174 S. W. 519.

People ex rel Jefferson vs. Smith (supra) was a case in which the right to tax mortgage securities, held outside the state was denied. The statute (2 R. S.—7th Ed.—981) read as follows:

"All lands and all personal estate within this State whether owned by individuals or by corporations shall be liable to taxation subject to the exemptions hereinafter specified."

The language of the court was in part as follows:

"The statute providing for the disposition of personal estate within this state was not intended to subject to taxation personal securities actually in another state, held, managed and controlled there, under the protection of the laws of that state, and subject to taxation there in the hands of agents. * *

"It is clear from the statutes referred to and the authorities cited and from the understanding of businessmen in commercial transactions, as well as jurists and legislators, that mortgages, bonds, bills and notes, have for many purposes come to be regarded as property and not as the mere evidence of debts, and that they may thus have a situs at the place where they are found like other visible tangible chattels."

The effect of the New York decisions so far as choses in action are concerned, was obviated by the passage of a statute (L. 1883 c. 392, Sec. 1) declaring that all debts however secured or wherever the security might be held should be deemed for the purpose of taxation personal estate within the state.

In Commonwealth v. West India Oil Refining Co., the defendant was a Kentucky corporation. All of its property was located in Cuba and Porto Rico. Its money was earned and kept there, and its accounts

were due and payable there. On these facts the county court held that the cash was not liable to taxation in Kentucky, but that the accounts were liable. On appeal to the circuit court, it was held that neither the cash, nor the deposit in the bank there, nor the accounts had a taxable situs in Kentucky. An appeal was taken to the Court of Appeals of Kentucky which not only affirmed the decision of the circuit court, but held that not only was this property not taxable as not being within the statute, but that Kentucky had no jurisdiction to tax, even if the property had been within the scope of the statute. The judgment of Hobson J., contained the following:

"For many purposes the domicile of the owner is deemed the situs of his personal property, but this is only a fiction from motives of convenience, and is not of universal application, but yields to the actual situs of the property when justice requires that it should, and is not allowed to be a controlling feature in matters of taxation."

In *Commonwealth v. B. F. Avery & Sons,* the defendant was a Kentucky corporation having its principal office in Kentucky and branches in five other states. It was held that accounts receivable at the branch offices were not taxable in Kentucky; but that they had a taxable business situs in the state of the branch offices.

Among the earlier Federal cases to which reference is most frequently made in the later cases is State Tax on Foreign-Held Bonds, 15 Wall. 300, decided in 1873. In that case it was held that the inter-

est on bonds of a domestic corporation owned by a non-resident could not be taxed at the domicile of the corporation. The decision is lengthy, but the following passage referring to *bonds* and *bank notes* is of particular interest on the subject in hand:

"It is undoubtedly true that the actual situs of personal property which has a visible and tangible existence, and not the domicile of its owner, will, in many cases, determine the State in which it may be taxed. The same thing is true of public securities consisting of State bonds and bonds of municipal bodies, and circulating notes of banking institutions; the former, by general usage, have acquired the character of, and are treated as, property in the place where they are found, though removed from the domicile of the owner; the latter are treated and pass as money wherever they are. But other personal property, consisting of bonds, mortgages and debts generally, has no situs independent of the domicile of the owner, and certainly can have none where the instruments, as in the present case, constituting the evidence of debt, *are not separated* from the possession of the owners."

It will be noticed that the bonds were in fact in the possession of the non-resident owner; also that the court had then got to the point of holding that State and municipal bonds as well as circulating bank notes had come to be regarded in this respect as on the same level with tangible personal property, but that that was as far as it thought it could go then, although it *at least suggested a question as to other securities when they were in fact separated from their owners.* That decision has later been discussed and narrowed down in many subsequent decisions,

and in Blackstone v. Miller, 188 U. S. 189, in which a debt and also a deposit with a trust company were involved, the court, with one dissenting vote, said with reference to that decision:

"The taxation in that case was on the interest on bonds held out of the State. *Bonds and negotiable instruments are more than merely evidence of debt.* The debt is inseparable from the paper which declares and constitutes it, by a tradition which comes down from more archaic conditions. Bacon v. Hooker, 177 Mass. 335, 337. Therefore, considering only the place of the property, it was held that bonds held out of the State could not be reached. The decision has been cut down to its precise point by later cases."

The taxable situs of *notes* and *mortgages* was involved in the case of New Orleans v. Stempel, 175 U. S. 309, (1899) and it was held that:

"Notes and mortgages, the owner of which is domiciled in another state, when they are kept within the state by an agent, may be subject to taxation by the laws of the state in which they are held."

Mr. Justice Brewer said:

"If we look to the decisions of other States we find the frequent ruling that when an indebtedness has taken a concrete form and become evidenced by *note, bill, mortgage* or *other written* instrument, and that written instrument evidencing the indebtedness is left within the State in the hands of an agent of the non-resident owner, to be by him used for the purposes of collection and deposit or reinvestment within the State, its *taxable situs is in the State.* See Catlin v. Hull, 21 Vermont, 152, in which the rule was thus announced (pages 159, 161): 'It is undoubtedly true that, by generally acknowledged principles of public law, personal chattels follow the person of the owner, and that upon his death, they are to be distributed according to the law of his domi-

cile; and in general, any conveyance of chattels, good by the law of his own domicile, will be good elsewhere. But *this rule is merely a legal fiction,* adopted from considerations of general convenience, and policy, for the benefit of commerce and to enable persons to dispose of their property, at their decease, agreeably to their wishes, without being embarrassed by their want of knowledge in relation to the laws of the country, where the same is situate.'"

See also Bristol v. Washington County, 177 U. S. 133, (1900) dealing with the taxation situs of *bonds* and *mortgages* belonging to a resident of New York, and held by an agent resident in Minnesota with authority to invest and reinvest the proceeds. It was decided that the securities were taxable in Minnesota. In the course of the decision Fuller, C. J., cited with approval the case of Re Jefferson, 35 Minn., 215, in which the Court, after discussing the doctrine *mobilia sequuntur personam,* says:

"For many purposes the domicil of the owner is deemed the situs of his personal property. This, however, is only a fiction, from motives of convenience, and is not of universal application, but yields to the actual situs of the property when justice requires that it should. It is not allowed to be controlling in matters of taxation. * * * * * *

"The obligation to pay taxes on property for the support of the government arises from the fact that it is under the protection of the government. Now, here was property within this state, not for a mere temporary purpose, but as permanently as though the owner resided here. It was employed here as a business by one who exercised over it the same control and management as over his own property, except that he did it in the name of an absent princi-

pal. It was exclusively under the protection of the laws of this state. It has to rely on those laws for the force and validity of the contracts on the loans, and the preservation and enforcement of the securities. *The laws of New York never operated on it.* If credits can ever have an actual situs other than the domicil of the owner, can ever be regarded as property within any other state, and as under obligation to contribute to its support in consideration of being under its protection, it must be so in this case."

See *Board of Assessors v. Comptoir National D'Escompte,* 191 U. S. 388, (1903).
Union Co. v. Kentucky, 199 U. S. 194, (mortgages and stocks).

Also,

Liverpool, London & Globe Insurance Co. v. Board of Assessors for Parish of Orleans, 221 U. S. 346 (1911) (Credits).

"When it is said that intangible property, such as credits on open account, have their situs at the creditor's domicile, the metaphor does not aid. Being incorporeal, they can have no actual situs. But they constitute property; as such they must be regarded as taxable, and the question is one of jurisdiction. *The legal fiction,* expressed in the maxim *mobilia sequuntur personam, yields to the fact of actual control elsewhere.* And in the case of credits, though intangible, arising as did those in the present instance, the control adequate to confer jurisdiction may be found in the sovereignty of the debtor's domicile. The debt, of course, is not property in the hand of the debtor; but it is an obligation of the debtor and is of value to the creditor because he may be compelled to pay; and control over the debtor at his domicile is control of the ordinary means of enforcement. Tested by the criteria afforded by the authorities we have cited, Louisiana must be deemed to have

had jurisdiction to impose the tax. The credits would have had no existence save for the permission of Louisiana; they issued from the business transacted under her sanction within her borders; the sums were payable by persons domiciled within the state, and there the rights of the creditor were to be enforced. *If locality, in the sense of subjection to sovereign power, could be attributed to these credits, they could be localized there. If, as property, they could be deemed to be taxable at all, they could be taxed there.*"

Also *Louisville & Jefferson Ferry Company v. Kentucky,* 188 U. S. 385, in which it was decided that a franchise granted by the proper authorities of Indiana, for maintaining a ferry across the Ohio River from the Indiana shore to the Kentucky shore, is an Indiana franchise, an incorporeal hereditament derived from, and having its legal situs for purposes of taxation in Indiana, *and not in Kentucky.*

The latest case in which this question has arisen in the Federal Courts is *De Ganay v. Lederer,* 239 Fed. 568. The Federal Income Tax Law of 1913 imposed the tax, so far as non-residents were concerned, upon the "entire net income from all property *owned* and every business, trade, or profession carried on *in the United States.*" Thus the statute is substantially the same as that in Hawaii. The question arose under that statute as to whether the income of a non-resident from *stock* and *bonds* of domestic corporations and *mortgages* in the hands of an agent in this country empowered to sell, assign and transfer them and to reinvest the proceeds, was subject to the tax,—on the theory that such stocks,

bonds and mortgages were "property owned * * * in the United States." The District Judge held that they were. Among other things he said:

"A bank note is but a promise to pay, but the concept of it soon changes to that of regarding it as itself concrete property, occupying space and having a situs. The same concept is readily extended to deposits in bank and to bonds, and indeed to what are known under the generic term of investments, mortgages and ground rents, and the like. They all come to be visualized, until they have an existence as real as that of physical things. Indeed it is allowable in common speech, and just as intelligible to speak of a person having ground rents in America, or indeed investments in America, as it is to say he had or owns a farm in America. * * * * * *

"Property is 'in' the United States when it can here be reached, whether the property be a house and lot, or whether it be bonds and mortgages.

"To return from these abstractions to the precise question before us, our conclusion is that this act of Congress, if read in the light of critical accuracy, does not tax the property on which this tax was levied; but if the language is interpreted in the light of the commonly accepted meaning of the words used, it does tax it, and the tax was properly collected."

Referring to the opinion of Mr. Justice Field in Foreign Held Bonds, 15 Wall. 300, above referred to, he continued:

"It is interesting to note (what was before not observed) that Mr. Justice Field, who delivered the opinion of the court, recognized that not only tangible personal property might have situs different from that of the domicile of the owner, but that state and municipal bonds and other forms of intangible property were recognized as in themselves physical property, and known as such in common speech, and

therefore also capable of having a situs of their own. He distinguished between municipal bonds, and the other property of like kind enumerated by him, and corporate bonds. This opinion was delivered in 1872. What was recognized by him as true of municipal bonds in 1872 seems to be equally true of corporate bonds and stocks in 1913. It would be an interesting confirmation of the observations hereinbefore made if public usage, which in 1872, included state and municipal bonds and bank notes among tangible possessions had progressed in 1913 to the point of embracing all stocks and bonds in the same classification."

The case was appealed to the Circuit Court of Appeals, which certified it to the Supreme Court. The latter (*De Ganay v. Lederer,* 250 U. S. 376) sustained the District Judge, basing its opinion in part upon the popular as distinguished from the technical construction of the statute and in part upon the fact that the stocks, bonds and mortgages were in fact in this country and were held by an agent which had considerable authority over them. The language of the court is in part as follows:

"We have no doubt that the securities, herein involved, are property. Are they property within the United States? It is insisted that the maxim *mobilia sequuntur personam* applies in this instance, and that the situs of the property was at the demicile of the owner in France. But this court has frequently declared that the maxim, a fiction at most, must yield to the facts and circumstances of cases which require it; and that notes, bonds and mortgages may acquire a situs at a place other than the domicile of the owner, and be there reached by the taxing authority. * * * * * *

"In the case under consideration the stocks and bonds were those of corporations organized under the laws of the United States, and the bonds and mortgages were secured upon property in Pennsylvania. The certificates of stock, the bonds and mortgages were in the Pennsylvania Company's offices in Philadelphia. Not only is this so, but the stocks, bonds and mortgages were held under a power of attorney which gave authority to the agent to sell, assign, or transfer any of them, and to invest and reinvest the proceeds of such sales as it might deem best in the management of the business and affairs of the principal. *It is difficult to conceive how property could be more completely localized in the United States.* There can be no question of the power of Congress to tax the income from such securities. Thus situated and held, and with the authority given to the local agent over them, we think the income derived is clearly from property within the United States within the meaning of Congress as expressed in the statute under consideration."

By the above case the status of stock certificates and bonds as property in themselves, and capable of having a "business situs" separate from the owner is definitely established; and the maxim that the situs of such property follows that of the owner, when it is separated from him, is clearly repudiated. This must be so for if the maxim had been followed then the intangible personalty of an alien resident of France could not possibly have been held to be "property in the United States." It is true as stated by the Court below (Record, p. 42) that the United States Supreme Court "did not infer that the *income* of such property would not have been taxable also at the domicile of the owner"; the question was not

even touched upon in the decision. The result however of the cases establishing the doctrine of "business situs" is, we submit, that when intangible property acquires such a situs, then, the reason for the general rule that such property has the situs of its owner because it has no other situs, failing, the rule itself yields, as it is well established it now does in the case of tangible property located in a foreign jurisdiction; and that such property is not *property in* the country where the owner has his domicile, and neither it nor the income thereof can be reached for taxation purposes *unless* the legislature of the owner's domicile expresses in appropriate language the intention to tax it wherever situate. (See the cases from New York, Kansas, Oregon and Kentucky above cited). As already pointed out this intention is manifested in various ways as, for example, by the use of expressions providing for taxation of property—or income derived from property—"within the state or elsewhere," "within or without the state," or "income from whatever source derived." The language of the Hawaiian act is not sufficient to cover the income of such property, and it must be borne in mind that *the Supreme Court of Hawaii has, in Hackfeld & Co. v. Luce, supra, committed itself to the proposition that notes and securities are taxable only in the jurisdiction in which they actually are, and that they have NO SITUS elsewhere.*

The De Ganay case is also direct authority in support of the contention made earlier herein that the language of the statute in Hawaii "property owned

in the Territory" refers to the location, and not to the ownership, of the property.

An attempt is made by the court below (Record, pp. 41, 42) to distinguish the De Ganay case from the case at bar by the fact that in the former the agent had a power of attorney which gave it authority to sell, assign and transfer the securities and reinvest the proceeds of sale as it might deem best, whereas in the latter the agents were apparently clothed only with authority to purchase and hold the securities, to collect the income and place it to the credit of the principal to be drawn upon from time to time as required. The court below overlooked the fact that the agents in the case at bar had evidently a power of sale, as the agreed facts show that the securities were held by the agent "until sold." We confess that we fail to see any distinction in the facts of the two cases that would localize or give the securities a business situs in the one and not in the other; in both cases the agent had physical possession of the securities with control over them for business purposes; the agent apparently had a power of purchase and sale, and also a power to collect the income.

II. It is submitted that none of the cases cited in its decision by the court below are authorities against the contentions made in the case at bar. In so far as they hold that bonds, negotiable instruments, certificates of stock, etc., are "only evidences of debt," e. g. Kirtland v. Hotchkiss, 100 U. S. 491,

they are in conflict with and are overruled by De Ganay v. Lederer. In Fidelity & Columbia Trust Co. v. Louisville, 245 U. S. 54, it appeared that moneys sought to be taxed were placed in another state to evade taxation (See 181 S. W. 1096, 1097) and the question of a business situs could not therefore arise. The only question involved in the majority of those cases was the *power* of the state to tax such property by the use of appropriate language; in all, (see for example Kirtland v. Hotchkiss, 100 U. S. 491; New Orleans v. Stempfel, 175 U. S. 309; Liverpool & London Globe Ins. Co. v. Board of Assessors, 221 U. S. 346) there was statutory warrant for the taxation, and it was the constitutionality of such statutes that was the object of attack.

Of that nature is the case of Maguire v. Trefry, 254 U. S. 12, cited by the Court below and termed the "controlling authority." This case we submit has no bearing whatsoever upon the question in the case at bar, viz.:

"Is the interest on the bonds, notes and deposits mentioned in the submission taxable under a statute which provides for the taxation only of the income derived from "property in the Territory?"

The case arose under a statute of Massachusetts in which it is provided:

"If an inhabitant of this commonwealth receives income from one or more executors, administrators or trustees, none of whom is an inhabitant of this commonwealth, or has derived his appointment from a court of this commonwealth, such income shall be subject to the taxes assessed by this act, according to

the nature of the income received by the executors, administrators or trustees,"

and the only question before the court was as to "the *right* of the state to tax the beneficiary of a trust at her residence although the trust itself may be created and administered under the laws of another state." (Id. p. 16.)

The case at bar raises no question as to the *right* of the Territory, if it so chooses, to tax the income of the securities and deposits under discussion, but only the question as to whether the legislature has in fact made such income taxable.

In concluding this branch of the case we submit: that by no principle of statutory construction can the income of the bonds, notes and deposits in question be brought within the language of the statute as income derived from "property within the Territory"; that the legislature by the use of the same language in respect to residents and non-residents (persons and corporations) intended that all should be on the same plane and that the income of property, and only property, which was actually within the Territory should be taxed; that the act should be construed in accordance with the practical construction which for over twenty-five years has been placed upon it by those charged with the duty of administering it; that the fiction embodied in the maxim *mobilia sequuntur personam* has never, so far as it relates to taxation, been adopted as part of the law of Hawaii, but has been emphatically repu-

diated and therefore cannot be read into the statute; that if that fiction has not been so repudiated the property in question had acquired a *business situs* on the mainland and therefore was not "property within the Territory" and the income therefrom is not taxable under the language of the present act; and that any doubt as to whether the income is taxable or not should be resolved in favor of the plaintiff-in-error.

For the reasons above stated we earnestly contend that the judgment of the Supreme Court of Hawaii should be reversed.

Respectfully submitted,

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APPENDIX.

ACT 65, SESSION LAWS OF 1896.

Section 1. From and after the first day of July, A. D. 1897, there shall be levied, assessed, collected and paid annually upon the gains, profits and income derived by every person residing in the Republic, and by every person residing without the Republic, from all property owned, and every business, trade, profession, employment or vocation carried on in the Republic, and by every servant or officer of the Republic, wherever residing, a tax of one per cent on the amount so derived; provided, that where the gains, profits or income of any such person who resides within the Republic, or of any servant or officer of the Republic wherever residing, shall not have exceeded the sum of Four Thousand Dollars for the preceding twelve months, only so much of such gains, profits or income as exceeds the sum of Two Thousand Dollars, shall be liable to such tax, and the tax herein provided for shall be assessed by the Assessors and Collectors for the time being for the several Tax Divisions of the Republic, and collected and paid upon the gains, profits and income for the year ending the 30th day of June next preceding the time for levying, assessing, collecting and paying the said tax.

Section 2. There shall be levied, assessed, collected and paid, except as herein otherwise provided, a tax of one per cent annually on the net profits or income above actual operating and business expenses

from all property owned, and every business, trade, employment or vocation carried on in the Republic, of all corporations doing business for profit in the Republic of Hawaii, no matter how or where created and organized; provided, however, that nothing herein contained shall apply to corporations, companies or associations organized and conducted solely for charitable, religious, educational or scientific purposes, including fraternal beneficiary societies, orders or associations operating upon the lodge system and providing for the payment of life, sick, accident or other benefits to the members of such societies, orders or associations, and dependents of such members, nor to insurance companies taxed on a percentage of the premiums under the authority of any other Act; nor to the stocks, shares, funds, real and personal property, or securities held by any fiduciary or trustee for charitable, religious, educational or scientific purposes.

Section 3. In estimating the gains, profits and income of any person or corporation, there shall be included all income derived from interest upon notes, bonds and other securities, except such bonds of the Republic of Hawaii, the principal and interest of which are by the law of their issuance exempt from all taxation; profits realized within the year from sales of real estate, including leaseholds for any term purchased within two years previous to the close of the year for which income is estimated; dividends upon the stock of any corporation; interest received or accrued upon all notes, bonds, mortgages

or other forms of indebtedness bearing interest whether paid or not, if good and collectable, less the interest which has become due from said person or corporation, or which has been paid by him or it during the year; the amount of all premiums on bonds, notes or coupons; the amount of sales of all movable property less the amount expended in the purchase or production of the same, and in the case of a person, not including any part thereof consumed directly by him or his family; money and the value of all personal property acquired by gift or inheritance, and all other gains, profits and income derived from any source whatever.

The net profits or income of all corporations shall include the amounts paid or payable to, or distributed or distributable among shareholders from any fund or account, or carried to the account of any fund or used for constructions, enlargements of plant, or any other expenditure or investment paid from the net annual profits made or acquired by said corporation.

In computing incomes, the necessary expenses actually incurred in carrying on any business, trade, profession or occupation, or in managing any property, shall be deducted, and also all interest due or paid within the year by such person or corporation on existing indebtedness. And all government taxes and license fees paid within the year shall be deducted from the gains, profits or income of the person who, or the corporation which, has actually paid the

same, whether such person or corporation be owner, tenant or mortgagor; also, losses actually sustained during the year incurred in trade or arising from fires, storms or shipwreck, and not compensated for by insurance or otherwise, and debts ascertained to be worthless.

Provided, that no deduction shall be made for any amount paid out for new buildings, permanent improvements, or betterments made to increase the value of any property or estate.

Provided, further, that where allowable herein only one deduction of two thousand dollars shall be made from the aggregate income of all the members of any family, composed of one or both parents, and one or more minor children, or husband and wife; that guardians shall be allowed to make a deduction in favor of each and every ward, except that in case where two or more wards are comprised in one family, and have joint property interest, the aggregate deduction in their favor shall not exceed two thousand dollars.

And provided, further, that in case where the salary or other compensation paid to any person shall not exceed the rate of two thousand dollars per annum, or shall be by fees, or uncertain or irregular in the amount or in the time during which the same shall have accrued or been earned, such salary or other compensation shall be included in estimating the annual gains, profits or income of the person to whom the same shall have been paid.

Provided, also, that in assessing the income of any person or corporation, there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of one per cent has been paid upon its net profits by said corporation as required by this Act, nor any gift or inheritance otherwise taxed as such.

ACT 20, SESSION LAWS OF 1901.

Section 1. From and after the first day of July, A. D. 1901, there shall be levied, assessed, collected and paid annually upon the gains, profits and income, over and above one thousand dollars, derived by every person residing in the Territory of Hawaii from all property owned, and every business, trade, profession, employment or vocation carried on in the Territory, and by every person residing without the Territory from all property owned, and every business, trade, profession, employment or vocation carried on in the Territory, and by every servant, or officer, of the Territory wherever residing, a tax of TWO PER CENT on the amount so derived during the year preceding.

Section 2. There shall be levied, assessed, collected and paid annually, except as hereinafter provided, a tax of TWO PER CENT on the net profit or income above actually operating and business expenses, from all property owned, and every business, trade, employment or vocation carried on in the Territory of Hawaii, of all corporations doing business

for profit in the Territory, no matter where created and organized; provided, however, that nothing herein contained shall apply to corporations, companies or associations conducted solely for charitable, religious, educational or scientific purposes, including fraternal beneficiary societies, nor to insurance companies taxed on a percentage of the premiums under the authority of another Act.

SECTION 3. In estimating the gains, profits and income of any person or corporation, there shall be included all income derived from interest upon notes, bonds and other securities, except such bonds of the Territory of Hawaii or of municipalities hereafter created by the Territory the principal and interest of which are by the law of their issuance exempt from all taxation; profits realized within the year preceding from sales of real estate, including leaseholds purchased within two years; dividends upon the stock of any corporation; the amount of all premiums on bonds, notes or coupons; the amount of sales of all movable property, less the amount expended in the purchase or production of the same, and in the case of a person not including any part thereof consumed directly by him or his family; money and the value of all personal property acquired by gift or inheritance, and all other gains, profits and income derived from any source whatsoever.

SECTION 4. The net profits or income of all corporations shall include the amounts paid or payable to, or distributed or distributable among sharehold-

ers from any fund or account, or carried to the account of any fund or used for construction, enlargements of plant, or any other expenditure or investment paid from the net annual profits made or acquired by said corporation.

In computing incomes, the necessary expenses actually incurred in carrying on any business, trade, profession or occupation, or in managing any property, shall be deducted, and also all interest paid by such person or corporation on existing indebtedness. And all government taxes and license fees paid within the year shall be deducted from the gains, profits or income of the person who or the corporation which has actually paid the same, whether such person or corporation be owner, tenant or mortgagor; also all losses actually sustained during the year incurred in trade or arising from losses by fire not covered by insurance, or losses otherwise actually incurred.

Provided, that no deduction shall be made for any amount paid out for new buildings, permanent improvements or betterments made to increase the value of any property or estate.

Provided further, that no deduction shall be made for personal or family expenses, the exemption of one thousand dollars mentioned in Section 1 being in lieu of same.

Provided further, that where allowable herein only one deduction of one thousand dollars shall be made from the aggregate annual income of all the

members of one family composed of one or both parents and one or more minor children, or husband and wife; that guardians shall be allowed to make a deduction in favor of each and every ward, except where two or more wards are comprised in one family, in which case the aggregate deduction in their favor shall not exceed one thousand dollars.

Provided further, that in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per cent has been assessed upon its net profits by said corporation as required by this Act, nor any bequest or inheritance otherwise taxed as such.

REVISED LAWS OF HAWAII, 1915.

SEC. 1305. RATE ON PERSON'S INCOME. There shall be levied, assessed, collected and paid annually upon the gains, profits and income over and above fifteen hundred dollars, derived by every person residing in the Territory of Hawaii, from all property owned, and every business, trade, profession, employment or vocation, carried on in the Territory, and by every person residing without the Territory from all property owned, and every business, trade, profession, employment or vocation carried on in the Territory, and by every servant or officer of the Territory, wherever residing, a tax of two per cent on the amount so derived during the taxation period as herein defined.

The taxation period within the meaning of this chapter shall be the year immediately preceding the first day of January of each year, in which such tax is payable.

SEC. 1306. ON CORPORATION INCOME. There shall be levied, assessed, collected and paid annually, except as hereinafter provided, a tax of two per cent on the net profit or income above actual operating and business expenses derived during each taxation period, from all property owned, and every business, trade, employment or vocation, carried on in the Territory of Hawaii, of all corporations, doing business for profit in the Territory, no matter where created and organized; provided, however, that nothing herein contained shall apply to corporations, companies or associations, conducted solely for charitable, religious, educational or scientific purposes, including fraternal beneficiary societies, nor to insurance companies, taxed on a percentage of the premiums under the authority of another law.

SEC. 1307. INCOME INCLUDES WHAT. In estimating the gains, profits and income of any person or corporation, there shall be included all income derived from interest upon notes, bonds and other securities, except such bonds of the Territory of Hawaii or of municipalities created by this Territory, the principal and interest of which are by the law of their issuance exempt from all taxation; profits realized within the taxation period from sales of real estate, including leaseholds purchased within two years;

dividends upon the stock of any corporation; the amount of all premiums on bonds, notes or coupons; the amount of sales of all movable property, less the amount expended in the purchase or production of the same, and in the case of a person not including any part thereof consumed directly by him or his family; money and the value of all personal property acquired by gift or inheritance, and all other gains, profits and income derived from any source whatsoever during said taxation period.

SEC. 1308 (as amended by Act 157, Session Laws of 1917). INCOME, HOW COMPUTED. The net profits or income of all corporations shall include the amounts paid or payable to, or distributed or distributable among shareholders from any fund, or used for construction, enlargement of plant, or any other expenditure or investment, paid from the net profits, made or acquired by said corporation, during the taxation period next preceding.

In computing incomes the necessary expenses actually incurred in carrying on any business, trade, profession or occupation, or in managing any property, shall be deducted, and also all interest paid by such person or corporation on existing indebtedness. And all government taxes, and license fees, paid within the taxation period next preceding shall be deducted from the gains, profits or income of the person who, or the corporation which, has actually paid the same, whether such person or corporation be owner, tenant or mortgagor; also all losses actually

sustained during the taxation period next preceding, incurred in trade, or arising from losses by fire not covered by insurance, or losses otherwise actually incurred, and including a reasonable allowance for exhaustion, wear and tear of property arising out of its use or employment in a business or trade; provided, however, that in no case shall such depreciation exceed the amount actually shown by and as written off the books.

Provided, that no deduction shall be made for any amounts paid out for new buildings, permanent improvements or betterments, made to increase the value of any property or estate.

Provided, further, that no deduction shall be made for personal or family expenses, the exemption of fifteen hundred dollars for each taxation period, mentioned in Section 1305, being in lieu of the same.

Provided, further, that where allowable under this chapter, only one deduction of fifteen hundred dollars for each taxation period shall be made from the aggregate annual income of all the members of one family, composed of one or both parents and one or more minor children, or husband and wife; that guardians shall be allowed to make a deduction in favor of each and every ward, except where two or more wards are comprised in one family, in which case the aggregate deduction in their favor shall not exceed fifteen hundred dollars for each taxation period.

Provided, further, that in assessing the income of any person or corporation there shall not be included the amount received from any corporation as dividends upon the stock of such corporation if the tax of two per centum has been assessed upon the net profits of such corporation as required by this chapter, nor any bequest or inheritance otherwise taxed as such.